

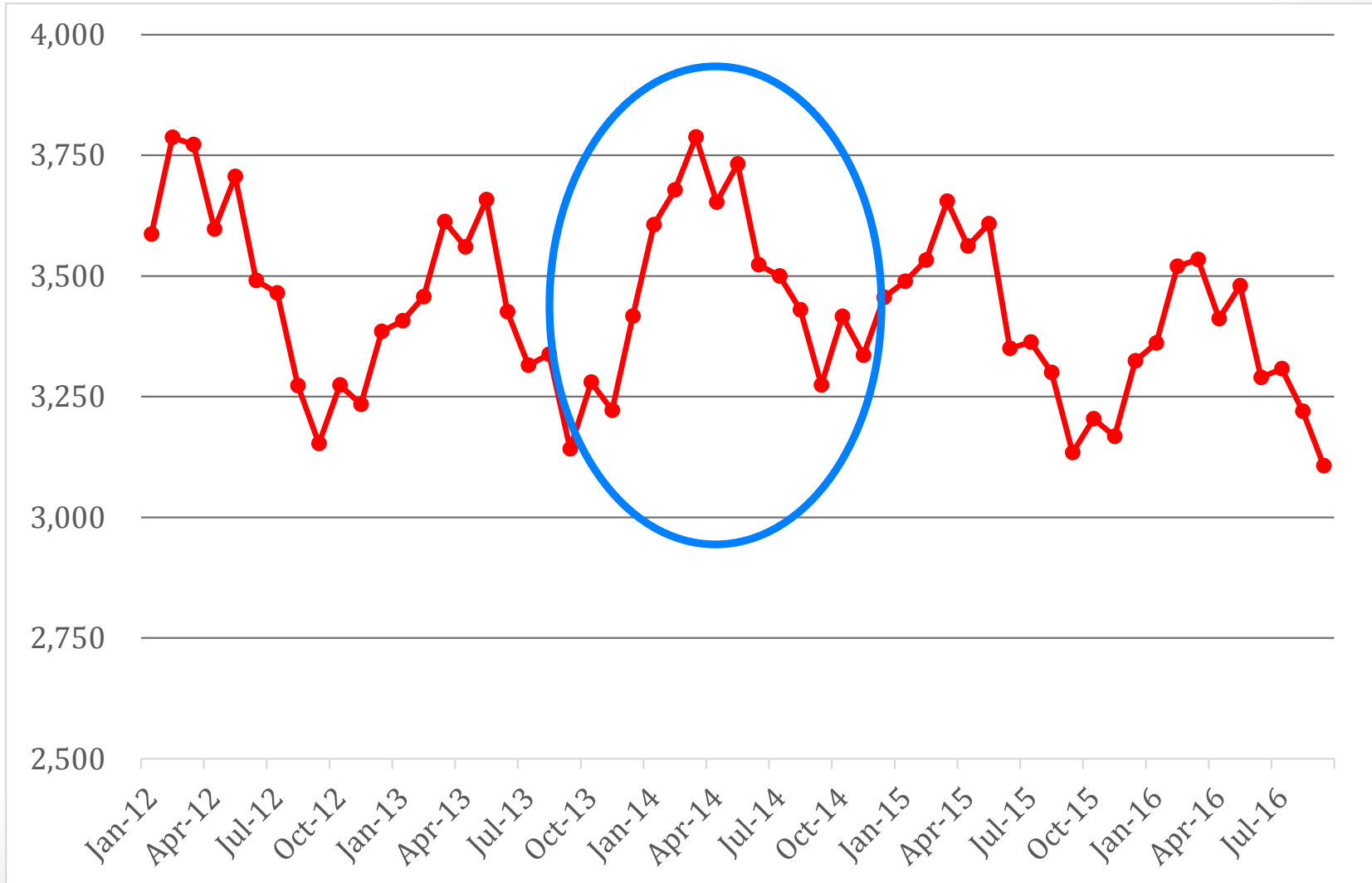
California Dairy Industry

Situation and Outlook

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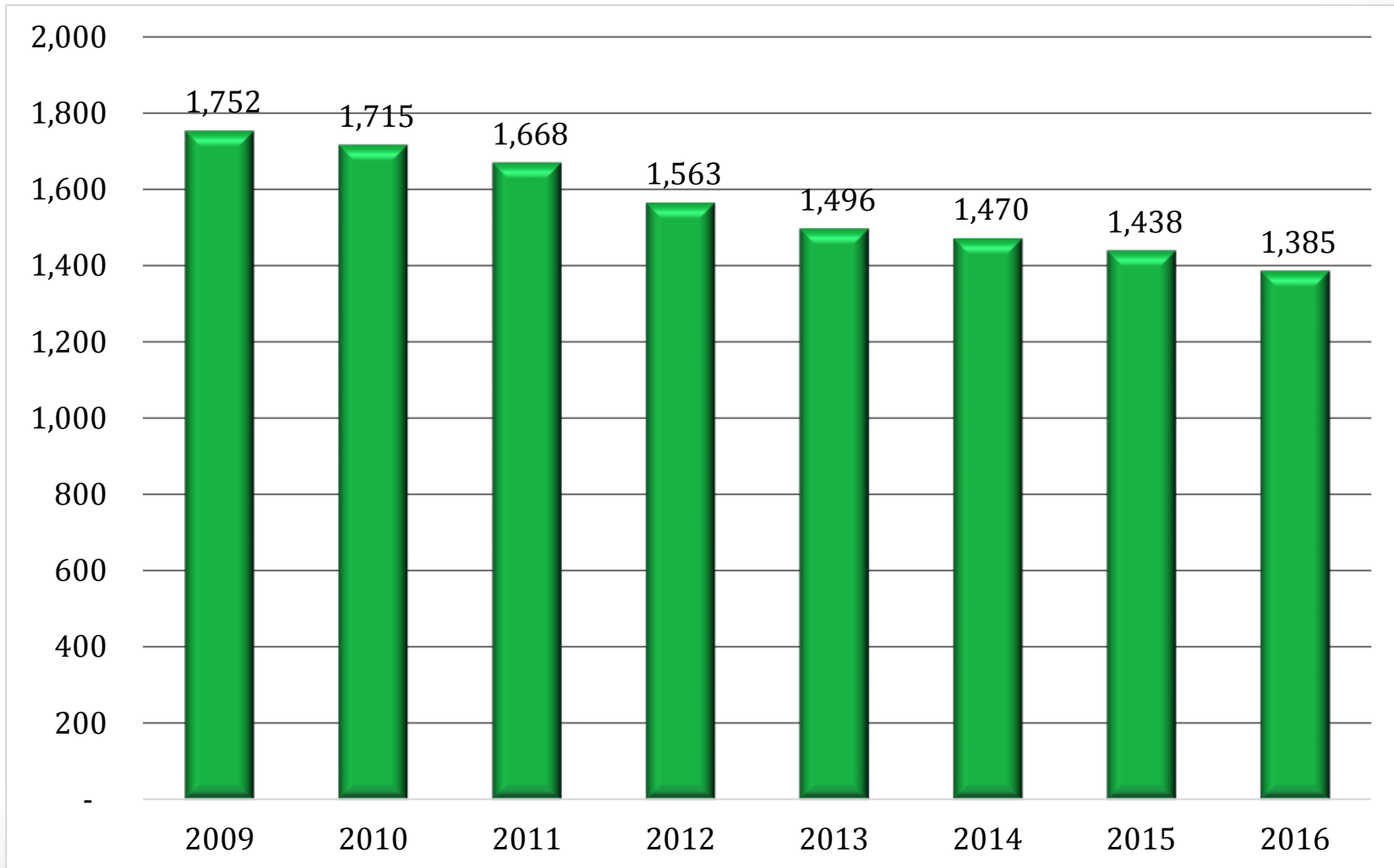
California Monthly Milk Production



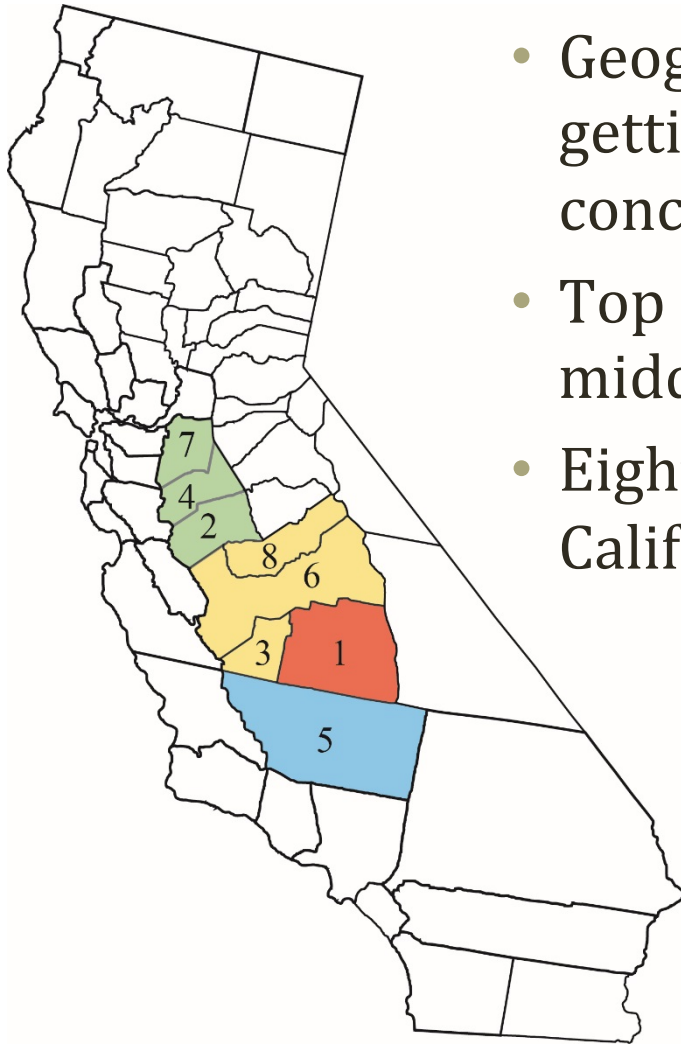
California Milk Price



Number of California Dairy Farms



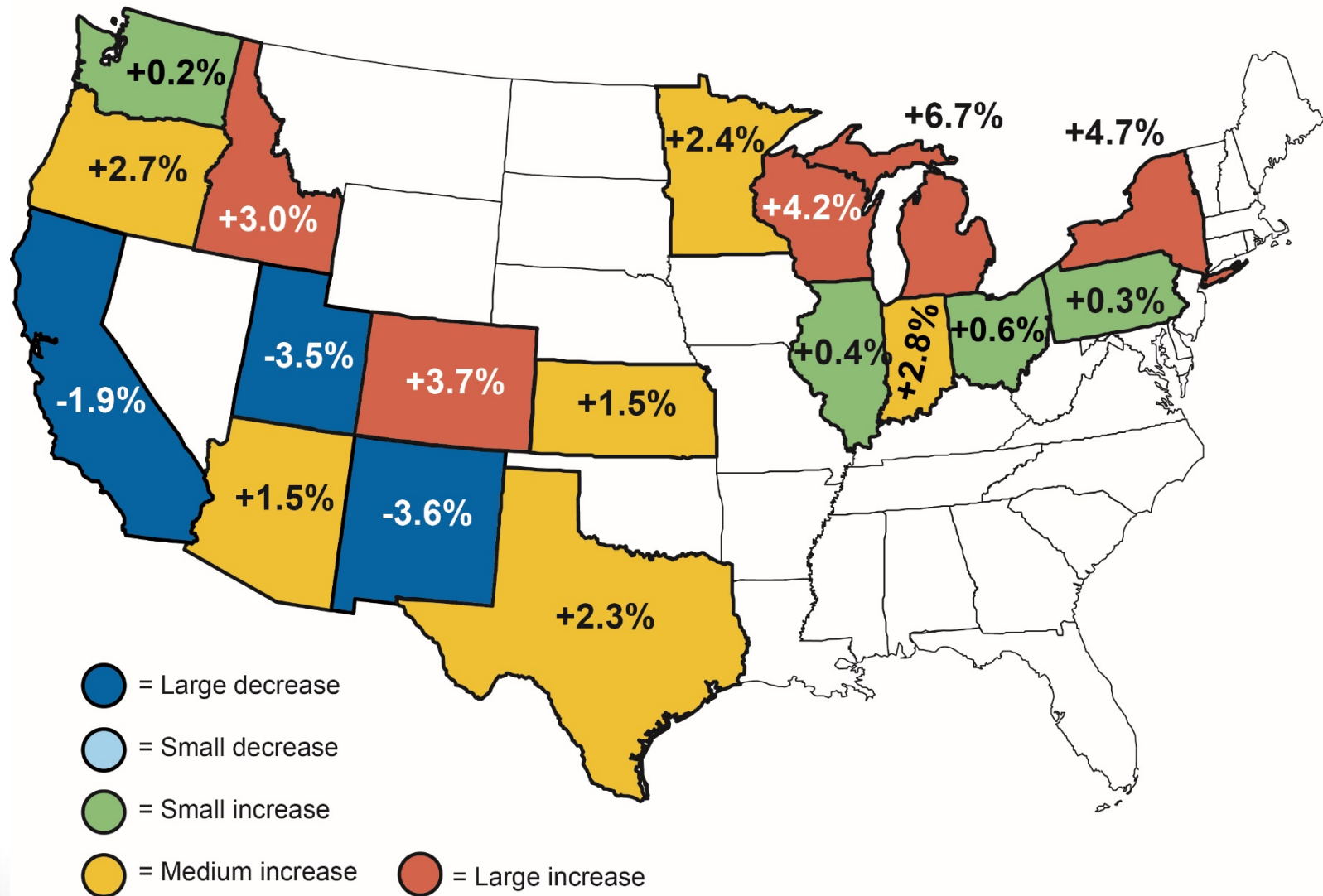
Location of Milk Supply



- Geographic footprint of milk is getting smaller and more concentrated in the Central Valley
- Top eight counties are all in the middle one-third of the state
- Eight counties produce 90% of California's milk

Where the dairy industry is hot and not

YTD 2016 Milk Production



Outlook for Dairy

- In two short years, the California dairy industry has completely changed
 - For decades, the industry struggled with balancing abundant milk supplies with processing capacity
 - Critical times for balancing milk supplies:
 - February through May
 - Thanksgiving to New Year's
 - Starting in late 2015, the opposite problem emerged, i.e., finding enough milk to keep assets running

Outlook for Dairy

- The foundation of the dairy industry is built on dairy farms and milk
- Three related and dependent sectors:
 - Farms to produce feed (many located out of state)
 - Milk processing plants to produce (and sell) dairy products
 - Affiliated businesses that are economically viable
- Widespread and growing concern about the alarming trends seen on the dairy farm side
- Dairy farms are just responding to economic signals and pressures

Outlook for Dairy

- What has changed in the last five to ten years?
 - Milk price stability has been altered as government involvement has decreased
 - Emergence of diversified operations – operate dairy farm but with some additional farming – reduces risk
 - Permanent crops were proven to be effective against down years for the dairy farm
- Environmental restrictions have been building over a period of years
 - Dairy farms and milk processing plants do not have the exemptions that they used to have

Outlook for Dairy

- What do the indicators suggest now?
 - Milk supplies will become less available in CA
 - Will have a stable and fixed asset base for milk processing
 - Increased competition – processing plants will be forced to be lock in milk supplies
 - Greater interest in having direct shippers instead of buying milk from a cooperative
 - Dairy cooperatives are expected to be competitive with other milk buyers

Outlook for Dairy

- Why are dairy coops important in CA?
- Historically, about 80% of CA milk has been marketed by dairy cooperatives
- Relevancy of milk marketing cooperatives?
- Keys to remaining relevant:
 - Continue to perform with good returns on capital investments
 - Offer services that cannot be found elsewhere
 - Consolidate to strengthen cooperative influence

Outlook for Dairy

- Survivability of dairy farming in CA
 - Must adapt to a different model than what grew the industry for decades
 - The next five years will not resemble the last five years
 - International markets have not proven to be predictably “good” for milk processors
 - Increased regulations for ag in general
 - Dairy industry will have additional regulatory problems to solve

Outlook for Dairy

- Survivability of dairy farming in CA (con' d.)
 - More competition for land, water and labor from other industries
 - Works well for dairies seeking options
 - Does not bode well for new dairy construction
 - On-farm margins will improve as competition for milk supplies heat up
 - Must be receptive to an increasingly inquisitive consumer base – “How is my food produced?”
 - For dairy farms that adapt, the future is bright